NATIONAL HOUSING LAW PROJECT

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Laurie Brimmer
Internal Revenue Service
Room 6526, 1111 Constitution Avenue NW.
Washington, DC 20224

RE: Comments to the Internal Revenue Service on 82 Federal Register 25047; Document Number 2017-11118; Proposed Collection; Comment Request for Regulation Project

Dear Ms. Brimmer:

On behalf of the low-income borrowers, residents, and communities that we represent, we have outlined specific areas for the Internal Revenue Service (IRS) to focus on in assessing compliance by developments funded through the Low Income Housing Tax Credit (LIHTC). The LIHTC program provides much needed resources to communities and neighborhoods in funding safe, stable, affordable housing. In order to enable the program to achieve this goal and minimize compliance issues that waste or abuse scarce program resources, the IRS should develop reasonable and clear rules to maintain long-term affordability and other compliance in funded developments.

With the issuance of Executive Orders 13777 and 13771, the IRS is tasked with reviewing existing regulations to identify rules that are "outdated, unnecessary, or ineffective" in order to make recommendations for regulations to "repeal, replace, or modify." (Executive Order 13777 sec. 3(d)). To assist the IRS with this process, we are submitting comments regarding regulations that are particularly ineffective in that have not sufficiently curbed LIHTC owners from seeking early release from their development's restrictive use agreements. In addition, they are ineffective, because the particular sections upon which we comment lack clarity or definition, making it difficult for HFAs to act.

Although we recognize that the large majority of developments are committed to maintaining affordability, modifications to these regulations would ensure that the express purpose of maintaining long-term affordable housing is not frustrated by some abusive owners seeking to take advantage of this essential program. This would also provide much needed guidance (including requirements, where appropriate) to the State agencies ultimately tasked with preventing such inappropriate early release.

Our greatest concern is with entities that appear to engage in strategic acquisition of LIHTC funded properties after the credits are already allocated (and, in many instances, already claimed) with the hope of avoiding the LIHTC use restrictions. These entities, unfortunately, are not the trusted partners of the housing finance agencies that are sensitive to their standing within the program, since they do not seek future allocations. Because such firms operate outside the Qualified Allocation Plan (QAP) process, one of the state's best incentives, eligibility for future credits, does not work. This is the perfect place for the IRS to step in and provide more detailed regulation. This specifically impacts the comments on planned foreclosure and qualified contracts below.

Here are regulatory modifications the IRS can make to maintain affordability and improve compliance:

1) The IRS must provide a system for providing prompt, publically available guidance to housing finance agencies seeking guidance on policy issues.

As you know, under the LIHTC program, state housing finance agencies have the obligation to monitor a development's compliance with the tax code. While the states have this on-the-ground obligation, the IRS still has ultimate obligation to administer the program. For example, states report non-compliance to IRS on Form 8823, but it is still the IRS's responsibility to impose sanctions.

Because the IRS operates the program but relies on the states for on-the-ground operations, the IRS must provide an avenue for questions and to address ambiguity. While we recognize that the IRS has a system of communication, it is not sufficient to address fast-moving, real life questions regarding developments, especially those seeking release from the program. We base this observation on our experience. In our work addressing and researching developments seeking early release, we have seen examples of state housing finance agencies asking for help but not receiving any clear guidance from IRS.

We believe that the IRS has a responsibility to provide publically available guidance on this federal program that affects millions of Americans. The IRS also has an obligation to improve the current ineffective system to protect federal resources, as well as the program's low-income intended beneficiaries.

2) The IRS should update the regulations regarding "early release" from affordability restrictions as they are "outdated, unnecessary, or ineffective."

The Internal Revenue Code permits developments to have early release from the LIHTC affordability guidelines in the event of a foreclosure or through the Qualified Contract (QC) process. Clarification is needed in order to ensure long-term affordability of LIHTC units and to clarify that these are the only circumstances that permit such a release.

The IRS should issue guidance on how to assess whether a foreclosure is a "planned foreclosure" and what must happen as a result.

As a general matter, there have been relatively few foreclosures of LIHTC financed properties. Unfortunately, however, we have seen instances in Michigan, New Jersey, Ohio, and in other states, that appear to be what the IRS has described as "planned foreclosures," i.e., actions by partners in LIHTC developments that are designed to result in a foreclosure, or deed-in lieu, and thus wipe out the affordability restrictions on these properties. Unfortunately, in these cases, it appears that the entity planning the foreclosure was not involved in the LIHTC application process and is not an entity that applies for credits. Instead, the entities buy into the development, loan themselves money through distinct but related companies, and then essentially foreclose on themselves after claiming that properties are unsuccessful. We are concerned that these are not isolated incidents, but rather what might be a growing business model. These concerns are not theoretical. A recent lawsuit filed in the Western District of Michigan describes an entity that appears to have engaged in planned foreclosures in several states. Complaint, Thompson v. Eenhoorn, LLC, 1:17-cv-00021 (W.D. Mich. Jan. 6, 2017).

These "planned foreclosures" both adversely impact the residents who live in these properties and may jeopardize public support for LIHTC. Anticipating this possibility of "planned foreclosures," Congress specifically gave the Treasury Secretary the authority to determine that such intentional transactions do not qualify as foreclosures that terminate the LIHTC affordability requirements. While the LIHTC program has been in existence for 30 years, the IRS has provided no guidance to allocating agencies as to how to deal with these situations. The IRS must use this opportunity to provide detail on how these transactions should be assessed. The implementation of Executive Orders 13777 and 13771gives the IRS the perfect opportunity to modify these ineffective regulations to ensure that planned foreclosures do not become a more popular business model that will lead to the permanent and premature loss of affordable rental housing. In addition, because planned foreclosure is not defined, this IRS guidance is ineffective, since the lack of definition or clarity makes HFA's waste precious resources trying to obtain guidance from the IRS (without success thus far) and trying to determine for themselves what that term means. Having the IRS provide guidance or definitions regarding the term planned foreclosure will reduce the ineffectiveness and inefficiency that inevitably accompanies ambiguity when terms are not defined

The IRS should modify the regulations to provide guidance on how agencies should evaluate requests for Qualified Contracts.

We are also seeing a problematic loss of affordable LIHTC developments through the Qualified Contract (QC) process outlined in the Internal Revenue Code. Through a public records request, we have learned of a significant number of units throughout Ohio that have been released prior to the end of their extended use period due primarily to the QC process. Other states have also experienced terminations under the QC process, unless they have required a waiver of this option by owners of LIHTC developments, as the Code permits.

While there are clearly steps that the state housing finance agencies can and should take to limit QCs, some may not do so, and others may do so ineffectively. To minimize waste and abuse of scarce public resources, the IRS should also provide further guidance in order to cease unnecessary QC transactions and to preserve much needed affordable housing. For example, the IRS should provide detail regarding what information a state housing finance agency should utilize to evaluate the request and the substantive considerations an agency must consider. It should also require tenant notification prior to any such QC termination so that tenants have an opportunity to provide input to the state agency. Furthermore, the IRS should also require that entities (and their affiliates) that pursue the qualified contract process should be subject to sanctions on subsequent LIHTC applications.

The IRS must provide further instruction to better ensure that developments are only released from use restrictions for the specific reasons stated in the Code.

As discussed above, the Internal Revenue Code only allows for a release of a development's affordability requirements in the event of a foreclosure or a qualified contract. Unfortunately, and contrary to the interest of the low-income tenants that the program was designed to serve, we have seen releases of developments or units for reasons outside of the specific ones specified in the Code. Our evidence is not simply anecdotal. Housing advocates focused on LIHTC issues have requested public records from housing finance agencies in several states. Based on our review of the information received, we have seen numerous developments or units released outside of the foreclosure or qualified contract contexts. Such releases are contrary to the Code and regulations. Thus, the IRS should provide further instruction regarding early release to better ensure that it will only be permitted in the event of foreclosure or qualified contracts. All considerations of release that comply with the Internal Revenue Code should still be subject to clear standards developed by the IRS or state agencies, including a transparent process that includes full and informed input from tenants and the affect local community.

3) The IRS should add regulations to address development compliance monitoring issues. Although State agencies are tasked with monitoring compliance, additional guidance is needed to ensure that properties are complying with regulations through the extended use period. During the initial ten year restrictive use period and the year five year recapture period, developments are less likely to have compliance issues as they are subject to losing tax credits. However, during the proceeding extended use period (which can last from fifteen to forty years depending on the State), it is incredibly difficult to encourage compliance as there are little penalties for failing to do so. Additionally it has been our experience that State agencies focus their compliance monitoring and enforcement during the initial fifteen year term. This is problematic given that a property is more likely to have compliance issues the longer it ages. Thus, we suggest that the IRS develop guidance or new regulations to mandate that state agencies plan for how they will ensure compliance throughout the entire restrictive use period.

Our interest in preserving quality affordable housing for low-income residents is consistent with the need to minimize waste, fraud and abuse in the LIHTC program, and the mission of state housing finance agencies and the program writ large to develop such housing and protect the public's investment. Thank you for considering our suggestions to promote these goals, and to preserve affordability.

We greatly appreciate the opportunity to submit comments on this important matter.

Sincerely,

National Housing Law Project

National Housing Trust

National Low Income Housing Coalition

Advocates for Basic Legal Equality

Legal Aid Society of Southwest Ohio

Legal Aid of Western Michigan

Michigan Poverty Law Program

Regional Housing Legal Services